# NFIB SMALL-BUSINESS NEWS



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## Recession Clouds over Main Street

**WASHINGTON, April 8, 2008** − Recession clouds appeared in the skies over Main Street, according to the most recent National Federation of Independent Business Small Business Economic Trends member survey. The NFIB Index of Small Business Optimism fell 3.3 points in March to 89.6 – its lowest reading since the monthly surveys were started in 1986, and the lowest quarterly reading since the second quarter of 1980. The decline was driven by a sour outlook for business conditions and real sales growth, accounting for half the decline in the Index. Weaker plans to create new jobs accounted for 21 percent of the decline. “We are seeing recession readings,” said NFIB Chief Economist William Dunkelberg.

| Optimism Components | Net % | Change |
|---|---|---|
| PLAN TO INCREASE EMPLOYMENT | 3 | -8 |
| PLAN TO INCREASE CAP. OUTLAYS* | 25 | -1 |
| PLAN TO INCREASE INVENTORIES | -2 | 0 |
| EXPECT ECONOMY TO IMPROVE | -23 | -14 |
| EXPECT HIGHER REAL SALES | -3 | -3 |
| CURRENT INVENTORY SATISFACTION | -1 | +3 |
| CURRENT JOB OPENINGS* | 19 | -1 |
| EXPECTED CREDIT CONDITIONS | -9 | -1 |
| NOW A GOOD TIME TO EXPAND* | 5 | -3 |
| EARNINGS TRENDS | -33 | -8 |

*Note: These components are measured as actual percentages of all respondents and are not net percentages. A net percentage is the percent positive minus percent negative.

In March, small business owners reported reducing employment an average of .12 employees per firm (seasonally adjusted), only half the reduction reported in February. Eight percent of the owners increased employment by an average of 3 workers per firm, and 15 percent reduced employment at an average of 4 workers per firm. Forty-six percent hired or tried to hire (unchanged, from February, down 11 points from last September). Seventy-eight percent of those trying to hire reported few or no qualified applicants for the job openings they were trying to fill.

“This is a much stronger labor market than typically found in a recession, although conditions could worsen from here,” Dunkelberg said.

Nineteen percent (seasonally adjusted) reported unfilled job openings, down a point from February (the 34-year average is 22 percent). Eight percent of the owners said the availability of qualified labor was their top business problem, down four points and indicative of a softening labor market and the elimination of some unfilled openings.

Over the next three months, 20 percent plan to create new jobs (down one point), and 7 percent plan workforce reductions (up three points), yielding a seasonally adjusted net 3 percent of owners planning to create new jobs – down eight points from February, the lowest reading since March 2003.

"Reductions in employment from layoffs and terminations eased from February," Dunkelberg said, "but the sharp decline in job creation plans does not bode well for economic growth in the near term."

The frequency of reported capital outlays over the past six months was down a point to a historically-weak 57 percent of all firms. Forty-one percent reported spending on new equipment (up a point), 17 percent acquired vehicles – down seven points – and 12 percent improved or expanded their facilities (down a point). Thirteen percent spent money for new fixtures and furniture (down two points), and 6 percent acquired new buildings or land for expansion.

The number of owners planning to make capital expenditures over the next few months fell a point to 25. Five percent said this is a good time to expand facilities, down three points from February. A net-negative 23 percent expect business conditions to improve over the next six months, down 14 points from February. A net-negative 3 percent expect increases in real sales, down three points.

Inventory reductions have continued into 2008 at a somewhat faster pace. More firms reported inventory reductions than gains by a seven-point margin (seasonally adjusted), five points worse than February. Unadjusted, 14 percent reported gains and 25 percent reported inventory reductions. A net-negative 1 percent of all firms reported stocks too low (seasonally adjusted), a three-point improvement from February. Dunkelberg said this suggests that the reduction process is near an end.

"Even with the weak outlook for sales, owners are fairly satisfied with current stocks," said Dunkelberg.

The net percent of owners expecting gains in real sales volumes lost three points, falling to a net-negative 3 percent, seasonally adjusted, historically a very low reading. Because of the pessimistic outlook for real sales volumes, more firms plan to continue to cut stocks rather than add to them, but at a pace no worse than in February. A net-negative 2 percent of all firms, seasonally adjusted, plan to add to stocks. Seasonally unadjusted, 16 percent plan to add to stocks while 13 percent will reduce them. Owners also plan to do less hiring and capital stock investing as a result.

The net percent of all owners (seasonally adjusted) reporting higher sales in the past three months lost three points, falling to a negative 11 percent. Unadjusted, 20 percent of all owners reported higher sales, and 40 percent reported lower sales, indicating that the economy is weak compared to six months ago.

A slowing economy is not deterring firms from raising prices. The net percent of owners reporting higher average selling prices rose another five points to a net 18 percent in March. The percent of owners citing inflation as their No. 1 problem rose four points to 12 percent, the highest reading since 1982. Plans to raise prices rose seven points to 29 percent of all owners. Unadjusted, 34 percent reported raising average selling prices, up three points, and 14 percent reported lower selling prices, down a point.

The percent of owners reporting earnings gains tumbled to its lowest level since early 2003. Seasonally adjusted, those reporting declining earnings outnumbered those with gains by 33 percentage points. Widespread price increases could not counter the pressures from higher costs and weaker sales. And, a net 24 percent of all firms reported raising average compensation – more than were able to pass these costs on in higher prices.

Of owners reporting higher earnings (14 percent, down two points), 50 percent cited stronger sales (down 10 points), and 7 percent credited higher selling prices. For those reporting lower earnings compared to the previous three months (53 percent, up eight points), 47 percent cited weaker sales (unchanged), and 17 percent cited higher materials costs (including energy). Four percent each cited higher labor costs, higher insurance costs, lower selling prices and higher taxes for the adverse performance of profits. There were no complaints about credit problems.

For the eighth straight month since the Federal Reserve declared the existence of a "credit crunch", no evidence of credit problems has appeared on Main Street. Regular borrowing activity was reported by 33 percent of the owners, down a point from February and typical of readings for the past 15 years. There is no evidence that cash flow problems have increased dependence on credit from the banking system.

Only 2 percent of the owners cited the cost and availability of credit as their No. 1 business problem (down a point), far from the record 37 percent reached in 1982 and unchanged for years. Thirty-two percent reported all their borrowing needs met (down three points) compared to 6 percent who reported problems obtaining desired financing (up two points). (The remainder did not want/need to borrow.) Perhaps the slight decline in borrowing signals a modest increase in difficulty. “Undoubtedly, some small businesses borrowed from branches of large Wall Street banks now short of capital to lend,” Dunkelberg said.

The net percent of owners expecting credit conditions to ease in the coming months was a seasonally adjusted net-negative 9 percent, a point worse than February (the average was negative eight in 2007). This indicates that more owners expect credit to tighten on Main Street in spite of the Fed’s expansionary policies.

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